

INTRODUCTION

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A little over twenty-five years ago, Congress passed the Bankruptcy Reform Act of 1978 (the "Reform Act").¹ Chapter 11 of the Code, named Reorganization, was the product of American experience under the Chandler Act of 1938.² The Chandler Act, which amended the Bankruptcy Act of 1898, grew out of the federal equity receiverships that saved the railroads. Chapter 11 melded certain aspects of Chapters X and XI of the Chandler Act. In the new, unified reorganization chapter, the debtor would remain in possession of, and operate its business during, the bankruptcy proceeding unless there was strong reason to replace the debtor. A right to adequate protection replaced the secured creditor's rights to its collateral and control over a case. A debtor could impose a plan on a creditor against its will. The absolute priority rule was made less absolute because a senior creditor could waive it by accepting a plan that did not give it absolute priority over junior parties. The Securities and Exchange Commission's role in the reorganization drama was reduced significantly.

The drafters hoped these changes would encourage companies to seek Chapter 11 relief in time to have a chance to reorganize. Consolidation of reorganization relief into a single chapter would eliminate the wasteful off-the-merits litigation regarding the appropriate relief chapter. Readjusting the balance of power between debtor and secured creditor would increase the likelihood of successful reorganization. According to its legislative history, Chapter 11 was also designed to permit a business to restructure its finances so it could continue to operate, employ workers, pay its creditors, and produce a return for its stockholders.

The premise of a business reorganization under the Reform Act is that assets used for production in the industry for which they were

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¹ The current law of bankruptcy is found in Title 11 of the United States Code. See 11 U.S.C. §§ 101 *et seq.* (2000). Its foundation is the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (effective Oct. 1, 1979) (codified as amended at 11 U.S.C. §§ 101 *et seq.* (2000)). References in this work to the "Code" are to Title 11 of the United States Code as amended through April 20, 2005.

² Chandler Act of 1938, Pub. L. No. 75-696, 52 Stat. 840, *repealed by* Bankruptcy Reform Act of 1978, Pub. L. 95-598, 92 Stat. 2549.

designed are more valuable than those same assets sold for scrap. Often, the return on assets that a business can produce is inadequate to compensate those who have invested in the business. Cash flow problems may develop and require creditors of the business, both trade creditors and long-term lenders, to wait for payment of their claims. If the business can extend or reduce its debts, it can often be returned to a viable state. It is thus more economically efficient to reorganize than to liquidate because it preserves jobs and assets.³

And so, with the Reform Act, the American experiment in bankruptcy law moved forward. Laws, however, are not the only things that change and laws, like war plans, often reflect what was, rather than what is. During the brief and, for some, glorious days of the 1980s and early 1990s, the nature of capital markets and business was changing. More and more, the manufacturing company employing several hundred people in a community was becoming less and less a reflection of postmodern American business. Service industries were replacing manufacturing enterprises. Financial markets were becoming increasingly global as well as more sophisticated and efficient. Investors were buying bankruptcy claims for pennies on the dollar, seeking a quick return on their investment. Instead of debtors using Chapter 11 to reorganize, secured creditors were using Chapter 11 to accomplish a federal foreclosure sale. The paradigm upon which Chapter 11 was imagined no longer reflected the reality of many businesses. Consequently, Chapter 11 was unresponsive to many postmodern distressed businesses, their creditors, and the world in which they operated.

Along with an increasing dissonance between the law of reorganization and the realities of the marketplace, Chapter 11 had its own internal problems. It was too expensive and cumbersome for small businesses to use it successfully. Big businesses who had "successfully" reorganized were reappearing at Chapter 11's doorstep to file a "Chapter 22" or "Chapter 33" case. Judicial reliance on the doctrine of necessity to authorize payment of "critical" vendors upset the Code's delicate distributive balance. Judicial reliance on the doctrine of substantive consolidation upset reasonable creditor expectations.

In the following pages, some of the country's finest bankruptcy minds discuss some of Chapter 11's thorniest issues, now further complicated by the overlay of the Bankruptcy Abuse Prevention and

³ H.R. REP. NO. 95-595, at 220 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6179.

Consumer Protection Act of 2005.⁴ Perhaps two different reorganization chapters are necessary after all: a general chapter and another specially tailored—streamlined—for small businesses? Perhaps investors need greater protection after all? Today's situation is reminiscent of the nineteenth-century pattern of bankruptcy legislation followed by repeal followed by new legislation followed by repeal. The late twentieth- and early twenty-first-century pattern is legislation followed by amendments followed by more amendments and more amendments after that. Both patterns reflect the ongoing difficulty of striking a proper balance between the interests of creditors and debtors in a constantly changing society that encourages risk-taking and incurring debt. These are exciting times because the genius of our legal system is its adaptability. This adaptability is a product of smart lawyers and judges devising creative responses to the latest set of challenges.

On behalf of all those who attended the Symposium on the Future of Chapter 11 or who read this issue of the *Boston College Law Review*, I thank both the American College of Bankruptcy and the *Boston College Law Review* for the privilege of listening to, and reading, some of our smartest lawyers' and judges' thoughts on Chapter 11.

⁴ Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (to be codified in scattered sections of 11 U.S.C., 12 U.S.C., 15 U.S.C., 18 U.S.C., and 28 U.S.C.).